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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of

Consumer Federation of America,	)	RM-9210
International Communications Association	)	
and National Retail Federation Petition	)	
Requesting Amendment of Reform and	)	
Price Cap Performance Review for	)	
Local Exchange Carriers	)	

OPPOSITION TO AND COMMENTS OF GTE

GTE Service Corporation and its affiliated domestic local exchange and interexchange telephone companies[1] (collectively "GTE") respectfully submit their opposition to, and comments on, the Petition for Rulemaking ("CFA Petition") filed by the Consumer Federation of America ("CFA"), the International Communications Association ("ICA"), and the National Retail Federation ("NRF") (collectively, "Petitioners"). Petitioners ask the Commission to initiate a rulemaking to immediately prescribe interstate access rates to cost-based levels. Since the Commission recently rejected a prescriptive approach, the Petition should be denied.

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[1] These companies include: GTE Alaska, Incorporated; GTE Arkansas Incorporated; GTE California Incorporated; GTE Florida Incorporated; GTE Hawaiian Telephone Company Incorporated; The Micronesian Telecommunications Corporation, GTE Midwest Incorporated; GTE North Incorporated; GTE Northwest Incorporated; GTE South Incorporated; GTE Southwest Incorporated; Contel of Minnesota, Inc.; and Contel of the South, Inc.; GTE Communications Corporation.

I. INTRODUCTION

In adopting the *Access Reform Order*,[2] the FCC set in motion a series of actions to move access prices to competitive levels. While GTE has argued that the Commission did not go far enough in removing implicit subsidies, creating a sustainable infrastructure of explicit subsidies and implementing pricing flexibility, the Commission's decision to reject a prescriptive approach to access reform as was urged by the interexchange carriers was correct. Indeed, recognizing the role price caps regulation and competition have played in causing access prices to migrate to economic cost levels, the Commission chose the proper alternative by rejecting a prescriptive approach.

Dissatisfied with the approach adopted in the *Access Reform Order,* CFA filed the Petition. The CFA Petition is based on two premises: First, competition for local service, nearly two years after the Act, is virtually non-existent; and second, appellate rulings have invalidated key components of the Commission's plan for local competition.

II. The FCC already rejected a prescriptive approach to access charges.

Many parties, including GTE, argued in the Access Reform proceeding that prescriptive approaches should be avoided because they would distort the market for access services and place undue burdens on Incumbent Local Exchange Carriers

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[2] *In the Matter of Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate and Structure and Pricing, End User Common Line Charges*, First Report and Order, CC Docket Nos. 96-262, 94-1, 91-213 & 95-72, FCC 97-158 (rel. May 16, 1997) ("*Access Reform Order*").

("ILECs") and regulators. Proposals to prescribe access rates lead unnecessarily to enormous tasks arising from the preparation, analysis and review of cost studies and re-initialization proceedings. These burdens are unwarranted and can only result in further market distortions and skew competitive entry by substituting the actions of regulators for the actions of the marketplace.

The FCC rejected a prescriptive approach in the *Access Reform Order* in favor of a market-based approach, though acknowledging that a market-based approach would take several years to accomplish the Commission's objectives. Petitioners argue the need for a prescriptive approach to access charges notwithstanding the FCC's finding less than a year ago that a market-based approach is reasonably designed to meet the FCC's objectives.[3] The FCC affirmed this position as recently as December 1997 in its Brief[4] filed in the U.S. Court of Appeals for the Eighth Circuit in support of the *Access Reform Order*. The CFA Petition shows nothing now that should change this assessment or require re-evaluation.

III. Petitioners distort the state of local competition and the need for FCC action.

Petitioners attempt to justify their argument that an immediate prescription of access rates is warranted by claiming that meaningful competition has not come about

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[3] MCI and others have challenged the same issues presented in the CFA Petition. *See* Joint Brief of Petitioners MCI Telecommunications Corporation, Cable & Wireless, Inc., and LCI International Telecom Corp., *Southwestern Bell Telephone Co. v. FCC*, No. 97-2866 *et al.* (8th Cir. filed, Oct. 28, 1997).

[4] Brief of Respondents, Federal Communications Commission, *Southwestern Bell Telephone Co. v. FCC*, No. 97-2618 *et al.* (8th Cir. filed, Dec. 16, 1997).

in the almost two years since the passage of the Telecommunications Act of 1996 ("the 1996 Act") and will not develop in the foreseeable future.[5] While it is understandable that Petitioners prefer to use the two-year interval to bolster their arguments, the *Access Reform Order* was adopted less than one year ago. The Commission correctly anticipated at that time a transition period to allow competitive forces to drive access pricing towards economic cost by setting a February 2001 date for incumbent price cap LECs to complete cost studies demonstrating their actual cost of providing interstate access services.[6] Petitioners are unreasonable in their expectations that the exceedingly complex *Access Reform Order* should be scrapped less than one year into the transition period.

Far from competition not developing in the foreseeable future, the mechanisms necessary for competitors to enter the local market are now in place and competitors are entering in ever increasing numbers. The special access markets have experienced strong competitive pressures for a number of years. According to statistics already available to the Commission in the NERA Pricing Flexibility White Paper, GTE has lost almost 19% of its DS1 facilities to competitive access providers ("CAPs") as of

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[5] Petition at 2. Petitioners argument that a prescriptive ratemaking is necessary because of the ILECs judicial challenge has undermined the Commission's policies is untenable. In challenging the Commission's orders, the ILECs prevailed in their arguments and avoided certain unlawful conditions as interpreted by the FCC. The ILECs clearly cannot be faulted for exercising their constitutional right of legal redress.

[6] Order at ¶¶267-8.

August 1997.[7] Similarly, going back to 1995, even before the *Access Reform Order* provided competitors with additional tools, the RBOCs experienced losses ranging from 22 to 50 percent in the most dense and competitive markets in the country.[8]

To suggest, as CFA does, that the ILECs are not sensitive to competition, completely ignores the facts. According to USTA, the RBOCs and GTE have spent more that $4 billion to open their markets to competition.[9] Nationwide, by October 1997, more than 1100 collocation cages have been erected, 3800 NXX codes have been assigned, more than 900,000 lines have been changed to competitors and more than 6,000 service requests have been processed daily by incumbent LECs.[10]

Petitioners such as CFA attempt to minimize these numbers, suggesting they are inconsequential considering size of the incumbents. However, the customers targeted by competitors are the high volume customers most responsible for significant revenues. The implications to revenue streams and the impacts on the remaining implicit subsidies are clear. Competition not only exists but is working in a manner that makes the implicit subsidies still in access charges unsustainable.

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7 *The Need for Carrier Access Pricing Flexibility in Light of Recent Marketplace Developments*, Richard Schmalensee and William Taylor, National Economics Research Associates (January 1998) at 19. ("NERA")

8 *Id.* at 20.

9 USTA Press release, October 22, 1997, "USTA Says Bell Companies And GTE Have Spent More Than $4 Billion To Open Their Markets To Competitors."

10 NERA at 22.

GTE disagrees completely with CFA's assessment of competition. As of January 13, 1998, GTE-affiliated ILECs have signed over 400 interconnection agreements pursuant to the 1996 Act in all 28 states in which they operate. GTE is currently negotiating with another 300 CLECs. These negotiations are expected to produce over 900 additional agreements before year-end 1998. Requests for negotiations continue to be received at a steady pace from CLECs of all sizes. During the Fourth Quarter of 1997, requests for negotiations increased in excess of 35% over the previous quarter. The mechanisms for competition mandated by the 1996 Act are in place. The Commission should allow the state commissions to complete their necessary review of those agreements and the market to accommodate the changing environment.

Competition is not only in place but rapidly accelerating. It would be shortsighted for the Commission to reverse course now and prescribe access rates. Rather, the Commission should continue to rely on market forces and accelerate its initiative to address pricing flexibility as expeditiously as possible, to assure the most competitive market environment.

IV. An immediate prescription based on forward-looking costs is unwarranted.

Petitioners argue further that the FCC should initiate action to impose access charges based upon forward-looking economic costs. While the Commission has consistently based its ratemaking on the principle of cost-based rates and cost-causation principles, nothing in the Act requires interstate rate levels to be tied to forward-looking cost.

Moreover, a forward-looking methodology does not reflect the actual cost of providing access services. While a forward-looking methodology looks at the cost of building anew, the reality is that the networks of today have evolved over the years and are made up of systems and equipment purchased years ago. Access charges must provide the opportunity to recover these actual costs.

The FCC already examined this issue thoroughly and determined in the *Access Reform Order* not to use forward-looking costs in determining access charges. Again, there is no justification for re-visiting this issue at this time.

V. A prescriptive approach to setting access rates at forward-looking costs amounts to a constitutional taking of ILEC property.

As GTE explained in its Comments in the Access Reform proceeding,[11] not only would a prescriptive approach undermine carrier incentives to invest in new technology and destroy efficiency incentives, setting access rates at forward-looking costs would result in a constitutional taking of ILEC property by failing to permit recovery of actual costs.[12]

In order to pass constitutional muster, the Commission must permit full recovery of prudently incurred costs that are assigned to the interstate jurisdiction. ILECs must be given the opportunity to recover two separate categories of costs: 1) under-recovered depreciation and 2) current, actual costs of operating the network that are

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[11] Comments of GTE, CC Docket 96-262, filed Jan. 17, 1997 at 80.

[12] U.S. Const. amend. V.

recorded in the regulated books of account pursuant to FCC rules. TSLRIC and TELRIC have utility only in determining whether certain rates are cross-subsidizing other rates in a multi-product firm; they are entirely unsuitable for setting prices. These methodologies intentionally fail to permit recovery of historical costs; grossly understate actual forward-looking costs; create profound disincentives to investment by ILECs and potential facilities-based competitors; and interfere with market forces by leaving no room for ILECs to adjust rates to respond to market conditions. These shortcomings are aggravated in the access market because TSLRIC and TELRIC do not account for the fact that current access rates include misallocations of costs to the interstate jurisdiction.

Failure to provide a reasonable opportunity for cost recovery would be an incontrovertible and unconstitutional taking of ILEC property. The historical cost recovery problem results directly from the long-standing regulatory compact between the FCC, the states, and ILECs under which ILECs agreed to uneconomic depreciation lives based on assurances that, over time, they would have the opportunity to recover their historical costs. Destroying that right in order to pave the way to competition is, undeniably, a taking.

Far from taking the unrealistic and indefensible u-turn leading to prescriptive regulation, the Commission must stay the course and earnestly pursue the historical cost recovery proceeding promised in the *Access Reform Order*.[13] As discussed above,

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[13] Order at ¶49.

the historical cost problem must be addressed before forward-looking costs can be realistically applied to access prices.

Although Petitioners argue that the American consumers should "pay charges that accurately reflect today's costs,[14] Petitioners completely ignore the fact that until the Commission addresses historical costs, today's costs include historical costs and these costs must be recovered.

VI. Petitioners fail to recognize the existence of prescriptive regulation in the *Access Reform Order*.

Although the Commission articulated a market-based approach to access reform, the *Access Reform Order* fell far short of the needed actions, such as pricing flexibility, to develop a competitive environment. While moving rates for non-traffic sensitive elements to a flat rate scheme, and to some extent reassigning costs to the cost causer, the Commission also took the clearly prescriptive action of establishing a uniform productivity factor of 6.0%, with a Consumer Productivity Dividend ("CPD") of 0.5%. This reduction in ILEC access charges, without regard to competition, actual ILEC productivity or any other demonstrable factor, has a clear prescriptive effect. In addition, the mandated access charge rate structure and treatment of exogenous adjustments in the *Access Reform Order* fall far short of a market-based approach.

Notwithstanding the strong showing by the ILECs for the need for pricing flexibility to promote efficient access pricing, the *Access Reform Order* failed to adopt policies permitting this flexibility. ILECs will only be able to compete effectively in the

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[14] Petition at 9.

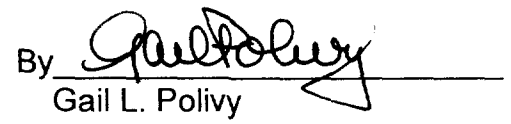
new marketplace if allowed to price with the same flexibility as their competitors. Not only should the Commission not hamstring ILECs with undue and intrusive regulatory constraints, it should allow the ILECs pricing flexibility to meet the 1996 Act's goal of robust competition. Removal of implicit subsidies through an adequate and competitively neutral Universal Service Fund, prompt treatment of the historical cost issue as promised in the *Access Reform Order*, pricing flexibility and a deregulatory environment, not prescriptive access charges, will ensure that rational pricing emerges and the proper economic signals are sent to both end users and telecommunications providers.

VII. CONCLUSION

For the foregoing reasons, GTE respectfully requests that the Commission deny Petitioners' request for an immediate prescription of access rates.

Respectfully submitted,

GTE Service Corporation its affiliated domestic local exchange and interexchange telephone companies

By 

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Certificate of Service

I, Ann D. Berkowitz, hereby certify that copies of the foregoing "Opposition to and Comments of GTE" have been mailed by first class United States mail, postage prepaid, on January 30, 1998 to the following parties:

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